

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE**

In re:)	Chapter 11
)	
ADVANTAGE HOLDCO, INC. et al.,)	Case No. 20-11259
)	
Debtors.)	(Jointly Administered)
)	

**RESPONSE TO DEBTORS' OBJECTION TO THE INCORRECTLY
CLASSIFIED CLAIMS OF ALLEGHENY CASUALTY COMPANY AND
INTERNATIONAL FIDELITY INSURANCE COMPANY**

Allegheny Casualty Company (“Allegheny Casualty”) and International Fidelity Insurance Company (“International Fidelity” and together with Allegheny Casualty, “IFIC”) files this Response to the Debtors’ Objection to the Incorrectly Classified Claims of IFIC (the “Claims Objection”) and states as follows:

BACKGROUND

1. On May 26, 2020 (the “Petition Date”), the debtors (together, the “Debtors”) filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code.

A. The Bonds, Indemnity Agreement, Cash Security and Letter of Credit

2. Prior to the Petition Date, the Debtors operated at airports nationwide under concession agreements negotiated with airport authorities or other supervising governmental entities (the “Airport Concession Agreements”). *See* Declaration of Alfred C. Farrell, Chief Financial Officer of Advantage Holdco, Inc., in Support of Chapter 11 Petitions and First Day Pleadings (the “Farrell Declaration”) (Dkt. #15) at ¶ 10.

3. Pursuant to the Airport Concession Agreements, the Debtors were typically granted a nonexclusive right to operate a car rental concession at a particular airport in exchange for a defined concession fee (the “Concession Fees”). *See* Debtors’ Motion (I) Authorizing, but not Directing,

Debtors to Continue to Operate their On-Airport Locations and Pay Prepetition Claims in the Ordinary Course; (II) Authorizing and Directing Banks to Honor Prepetition Checks and Fund Transfers for Authorized Payments, and (III) Granting Related Relief (the “Airport Motion”) (Dkt. # 12) at ¶ 7.

4. Generally, these Airport Authorities required that the Debtors obtain surety bonds to secure their obligation to pay these Concession Fees. Airport Motion, ¶ 13. Based on the terms of each surety bond, an Airport Authority was generally named as a bond obligee. Airport Motion, ¶ 14. If a valid claim was later filed against a surety bond, the surety company would pay the claim and then, based on its rights of indemnity and subrogation, seek reimbursement from the Debtors directly or based on any collateral.

5. For a number of these Airport Concession Agreements, the Debtors obtained surety bonds from IFIC (the “Bonds”) in connection with a General Agreement of Indemnity dated March 12, 2015 (the “Indemnity Agreement”) executed by and between the Debtors and IFIC. A true and correct list of these Bonds with an analysis of the gross exposure is attached as Exhibit A. A true and correct copy of the Indemnity Agreement is attached as Exhibit B.

6. The Indemnity Agreement creates a contractual right of indemnification and/or right of exoneration (in the form of collateral) on behalf of IFIC inclusive of any fees and costs incurred by IFIC. *See* Indemnity Agreement, § 2.

7. The Indemnity Agreement expressly states that any such amounts owed in connection with the Indemnity Agreement shall be “promptly” paid and that “[p]ayments not made...within 10 days after demand...shall bear interest[.]” *See* Indemnity Agreement, § 2

8. The Indemnity Agreement provides that “the Debtors shall deposit with the Surety on demand an amount of money or other collateral security acceptable to the Surety...and Surety shall have the right to use the [collateral security] or any portion thereof[.]” *See* Indemnity Agreement, § 3.

9. In connection with the Bonds and the Indemnity Agreement and as security for the IFIC's suretyship, certain of the Debtors caused the issuance of an Irrevocable Standby Letter of Credit pre-petition in favor of IFIC in the amount of \$1,750,000 (together with any amendment or modification thereto, the "Letter of Credit").

10. As the Debtors are aware, IFIC has partially drawn down on the Letter of Credit in the amount of \$500,000 which amount it continues to hold as security, to the extent not already applied by IFIC.

B. The Final DIP Order

11. The Final Order (I) Authorizing Debtor to Obtain Post-Petition Secured Financing Pursuant to 11 U.S.C. §§ 105, 361, 362 and 364; (II) Granting Liens and Super-Priority Claims; and (III) Granting Related Relief (the "Final DIP Order") contains the following language:

(a) Nothing in the Interim Order, **this Final Order or the Motion shall in any way *prime or affect the rights of International Fidelity Insurance Company or Allegheny Casualty Company* or their past, present or future parents, subsidiaries or affiliates (the "Surety") as to: (i) *any funds it is holding and/or being held for it presently or in the future, whether in trust, as security, or otherwise, including any proceeds due or to become due any of the Debtors or their non-debtor affiliates in relation to contracts bonded by the Surety*; (ii) any substitutions or replacements of said funds including accretions to and interest earned on said funds; or (iii) *any letter of credit (and any proceeds thereof) related to any indemnity, collateral trust, bond or agreements (including any and all amendment(s) or modification(s) thereto) between or involving the Surety and any of the Debtors or any of the Debtors' non-debtor affiliates* (collectively, (i) to (iii) the "Surety Assets"). **Nothing in the Interim Order, this Final Order or Motion shall affect the rights of the Surety under any *current or future indemnity, collateral trust, or related agreements between or involving the Surety and any of the Debtors or any of the Debtors' non-debtor affiliates as to the Surety Assets or otherwise, including, but not limited to, the Agreement of Indemnity* executed by Advantage Opco, LLC and Advantage Holdco, Inc., on or about March 12, 2014...**Nothing herein is an admission by the Surety or the Debtors, or a**

determination by the Bankruptcy Court, regarding any claims under any bonds, and the Surety and the Debtors reserve any and all rights, remedies and defenses in connection therewith. **Notwithstanding anything herein to the contrary, and subject to the terms herein, the Debtors hereby agree that, during the pendency of these proceedings, the Debtors shall, in accordance with and subject to applicable law, reimburse the Surety for attorneys' fees incurred and to be incurred by the Surety in accordance with the terms of any agreement among the parties.** For certainty, any Surety Assets that are not Surety Collateral shall be subject to the terms of this Final Order in all respects.

(b) Notwithstanding anything herein to the contrary, the Surety agrees that, if, as determined in the discretion of the Surety or the Court, **the Surety's aggregate gross exposure under any and all active and inactive bonds, plus up to \$200,000 for reasonable and documented expenses and attorneys' fees incurred and to be incurred by the Surety, plus any and all unpaid premiums, and plus any and all losses, costs and/or expenses incurred or to be incurred by the Surety under any active or inactive bonds, and to the extent that the amounts recoverable from any letter of credit (or the proceeds thereof) delivered to secure any Debtors' performance under an agreement between the Surety and any Debtor are equal to or less than the value of any letter of credit or proceeds thereof, then the Surety's only recourse for recovery of sums due or which may become due the Surety under or in connection with any indemnity agreement, bond or similar instrument shall be the letter(s) of credit and the proceeds thereof, provided that the Surety is able to successfully draw on said letter of credit and receive the proceeds thereof.**

Final DIP Order, § 26 (emphasis added).

12. Based on the Final DIP Order, the Debtors are obligated to comply with the terms of the Indemnity Agreement and further agreed to recognize any liens or trust fund claims held by IFIC or a Bond obligees (the "Bond Obligees" or each a "Bond Obligee") cannot be primed. *Id.*

13. The Debtors further agreed to reimburse IFIC for attorneys' fees and costs (together, the "Legal Fees") incurred and to be incurred in accordance with the terms of any agreement among the parties including the Indemnity Agreement. *See* Final DIP Order, § 26(a).

14. Notwithstanding the foregoing, section 26(b) of the Final DIP Order provides for an exception to the Debtors obligation to directly reimburse IFIC for its Legal Fees. Specifically, if, as determined in the discretion of IFIC or the Court, IFIC's aggregate gross exposure under the Bonds, plus up to \$200,000 for reasonable and documented Legal Fees, plus any and all unpaid premiums, and plus any and all losses, costs and/or expenses incurred or to be incurred by IFIC under the Bonds, and to the extent that the amounts recoverable from the Letter of Credit (or the proceeds thereof) are equal to or less than the value of Letter of Credit (or the proceeds thereof), then IFIC's only recourse for recovery of sums due or which may become due shall be the Letter of Credit (or the proceeds thereof), provided that the Surety is able to successfully draw on the Letter of Credit and receive the proceeds thereof. *See* Final DIP Order, § 26(b) (emphasis added).

15. Neither IFIC nor the Court has made the determination in section 26(b) of the Final DIP Order. Thus, the Debtors are obligated to promptly pay IFIC's Legal Fees. *See* Final DIP Order, § 26(a). Indeed, the Debtors have acknowledged as much. *Id.*; *see also* Exhibit C which is a true and correct copy of an email from Debtors' counsel acknowledging this obligation.

C. Basis of IFIC's POCs

16. On September 21, 2020, the Court entered a bar date as October 23, 2020 for both General Claims and Administrative Expense Claim for claims arising subsequent to the Petition Date but on or before September 30, 2020 (the "Administrative Claims Period").

17. By October 23, 2020, IFIC filed proofs of claims ("Proofs of Claims") against each of the Debtors asserting that specific portions of the claims were entitled to be treated as a secured claim. *See* Proofs of Claims ## 10189, 10191, 10193, 10195 – 10198, 10199 – 10200, 10202, 10204 – 10207. These POCs also assert general unsecured claims. *Id.*

18. On these Proofs of Claims, these secured claims are based on setoff/recoupment rights of IFIC, or any such rights of obliges, as well as lien rights of obliges, to which IFIC is subrogated.

19. By October 23, 2020, IFIC also filed administrative expense claims (“Administrative Expense Claims”) for amounts arising during the Administrative Claims Period. *See* Proofs of Claims ## 20004- 20011, 20013 – 2018.

20. These Administrative Expense Claims were based on (a) premiums incurred during the Administrative Claims Period; (b) Bond claims arising during the Administrative Claims Period; (c) attorneys’ fees and costs incurred by IFIC during the Administrative Claims Period; and (d) to the extent IFIC is subrogated to any Bond Obligee holding an administrative expense claim.

D. The Claims Objection

21. On November 10, 2021, the Debtors filed an Objection to the Incorrectly Classified Claims of International Fidelity Insurance Company and Allegheny Casualty Company (the “Claims Objection”) to the Proofs of Claims (Dkt. #1026).

22. Pursuant to the Claims Objection, the Debtors seek to reclassify the entirety of Proofs of Claims as general unsecured claims.¹

23. With respect to its secured claims, the Debtors alleges that IFIC relies on the Letter of Credit to claim a secured claim. Claims Objection, ¶¶ 16, 20. As it is not property of the estate, the Debtors argue IFIC cannot have a secured claim. *Id.*

24. With respect to its administrative expense claim, the Debtors allege (a) that IFIC does not and cannot identify any post-petition transaction with the estates arising out of a right of subrogation or

¹ The Debtors further seek to prejudice IFIC by arguing it has not produced all the Bonds when the request for the Bonds was made only a few days before the filing of this Claims Objection.

indemnity except for Legal Fees and (b) that IFIC has failed to explain how these Legal Fees and any such other post-petition amounts benefit the estate. Claims Objection, ¶¶ 22, 24 – 26.

25. Moreover, the Debtors allege that IFIC waived its right to recover against the Debtors and the estates if its Legal Fees can be satisfied by the Letter of Credit. *Id.*, ¶ 28. The Debtors further allege that it is not ripe to make this determination as the total value of IFIC's claims has yet to be determined. *Id.*

Basis of Response

26. The Debtors wrongly state that IFIC bases its secured claim on the Letter of Credit even though the Letter of Credit is not property of the estate. Instead, IFIC bases its secured claim on (i) its right of setoff that is preserved under the Bankruptcy Code and (ii) any secured claim (whether based on setoff and/or lien rights) held by a Bond Obligees to which it is subrogated.

27. The Debtors further err as to IFIC's administrative expense claim.² There are clearly post-petition transactions that have arisen and may still arise in connection with the Bonds. The Bonds clearly benefited the estate during the Administrative Claims Period as the Bond Obligees required

² The Debtors contradict themselves in their objection saying in one point all bonded post petition obligations are paid while acknowledging elsewhere that a post-petition claims of Dallas Fort Worth has not been paid putting in question the accuracy of their allegations. Moreover, the operating reports for different months show different amounts owed for this obligations. See Monthly Operating Reports (Dkt. ## 930, 948). While IFIC has asked why this is, the Debtors have not provided a response on this.

these Bonds as a condition for maintaining the Airport Concession Airports. As demonstrated in Exhibit A, IFIC's exposure exceeds the amount that would excuse the Debtors from satisfying IFIC's Legal Fees based on the limitation provided in Section 26(b) of the Final DIP Order. Furthermore, IFIC is also entitled to any administrative expense claim held by a Bond Obligee to which it is subrogated.

RESPONSE

A. IFIC is Entitled to a Secured Claim

28. IFIC is a secured creditor by way of its rights of setoff and recoupment. The law is first clear that such rights may not be disturbed.

29. Recoupment, a creditor's right long recognized in bankruptcy proceedings, is not in the nature of a mere lien, but is a defense to a claim for payment. *Lee v. Schweiker*, 739 F.2d 870, 875 (3d Cir. 1984) (“[W]here the creditor's claim against the debtor arises from the same transaction as the debtor's claim, it is essentially a defense to the debtor's claim . . .”). In other words, the recoupment is used to determine the proper liability on amounts owed. *Reiter v. Cooper*, 507 U.S. 258, 265 n. 2 (1993); *In re Holford*, 896 F.2d 176, 178 (5th Cir. 1990).

30. Setoff “gives a creditor the right ‘to offset a mutual debt owing by such creditor to the debtor,’ provided that both debts arose before commencement of the bankruptcy action and are in fact mutual.” *In re University Medical Center*, 973 F.2d 1065, 1079 (quoting *In re Davidovich*, 901 F.2d 1533, 1537 (10th Cir. 1990)). While setoff rights are defined and delineated by applicable non-bankruptcy law, the Bankruptcy Code recognizes and preserves these rights: “11 U.S.C. § 553(a) provides that, with certain exceptions, whatever right of setoff otherwise exists is preserved in bankruptcy.” *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 18 (1995); see also *In re Luongo*, 259 F.3d 323, 333 (5th Cir. 2001) (“It is impossible for us to ignore the clear statement of § 553 that this

title. . . does not affect any right of a creditor to offset . . .”). Hence, setoff gives rise to a secured claim.

31. IFIC also has a secured claim by way of subrogation to any Bond Obligees that possess a secured claim (whether by setoff/recoupment or lien rights). IFIC has an equitable subrogation right that arises by common law to the extent that Surety pays any claim under any of the bonds it has issued, including the Bonds.

32. Courts have recognized that a surety, upon payment of bond claims, is subrogated to the rights of the obligee on the bond. *See Pearlman v. Reliance Ins. Co.*, 371 U.S. 132, 135-36 (1962) (“there are few doctrines better established than that a surety who pays the debt of another is entitled to all the rights of the person he paid to enforce his right to be reimbursed”); *Henningsen v. United States Fid. & Guar. Co.*, 208 U.S. 404, 410 (1908) (holding surety has superior equity under the doctrine of subrogation in sums due under the contract after the surety made payments to beneficiaries/claimants under the bond where the bond principal failed to do so); *Prairie State Nat’l Bank v. United States*, 164 U.S. 227, 232-33 (1896) (holding surety had subrogation rights to contract funds after satisfying bonded obligations); *Ky. Cent. Ins. Co. v. Brown (In re Larbar Corp.)*, 177 F.3d 439, 443 (6th Cir. 1999) (noting “[t]he law is clear” that a surety’s right to subrogation arises “when a [bond principal] defaults on its obligations and a surety completes the work called for by the contract and pays all of the related bills”); *Nat’l Shawmut Bank of Boston v. New Amsterdam Cas. Co.*, 411 F.2d 843, 848-49 (1st Cir. 1969) (noting that upon bond principal’s default, the surety is subrogated to the obligee’s right to pay beneficiaries under the bond (in this case, laborers and materialmen), and to apply earned but unpaid progress payments at the time of default to the cost of completion of bonded obligations); *Mendelsohn v. The Dormitory Authority of N.Y. (In re QC Piping Installations, Inc.)*, 225 B.R. 553, 562 (Bankr. E.D.N.Y. 1998) (“it is now irrefutable that a surety, after satisfying its obligations under either a

payment or performance bond, is subrogated to the rights of the party he paid”); *John’s Insulation, Inc. v. Hartford Accident & Indem. Co. (In re John’s Insulation, Inc.)*, 221 B.R. 683, 688 (Bankr. E.D.N.Y. 1998) (noting that a surety, after completing a contract upon the default of the principal, is “subrogated to the rights of the principal, and has rights to the funds that are due and are to become due under a contract, including any undisbursed proceeds previously earned and any retainages held until contract completion”). In other words, a surety may step into the shoes of these entities and enforce the claims they may have against each other, or other third parties and the Plan should not encroach on a surety’s rights. Thus, IFIC has a secured claim to the extent it is subrogated to the rights of any Bond Obligor that possesses a secured claim (whether by setoff/recoupment or lien rights).

B. IFIC is Entitled to Administrative Expense Claims

33. Based on its rights of subrogation, IFIC has an administrative expense claim to the extent it is subrogated to the rights of any Bond Obligor that possesses one. However, IFIC also possess administrative expense claims of its own.

34. In this regard, pursuant to §§ 503(a) and (b) of the Bankruptcy Code, IFIC is entitled to receive payment for postpetition services rendered as an administrative expense claim.

Section 503(a) and (b) provide as follows:

(a) An entity may timely file a request for payment of an administrative expense, or may tardily file such request if permitted by the court for cause.

(b) After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title, including –

(1) (A) the actual, necessary costs and expenses of preserving the estate . . .

11 U.S.C. §§ 503(a) and (b).

35. The principal purpose of § 503(b)(1)(A) is to give creditors the incentive to continue dealing with the debtor-in-possession and supply it goods and services. *See e.g., In re Southern Soya Corp.*, 251 B.R. 302 (Bankr. D. S.C. 2000) (citing *Merry-Go-Round Enter. v. Simon DeBartolo Group (In re Merry-Go-Round Enter.)*), 180 F.3d 149, 158 (4th Cir. 1999)). In order for a claim to be granted administrative expense status, the party claiming entitlement to such status must establish: (1) that the claim arose out of a transaction between the creditor and the bankrupt's trustee or debtor-in-possession; and (2) that the claim directly and substantially benefited the estate. *See In re Merry-Go-Round Enter.*, 180 F.3d at 157; *Microsoft Corp. v. DAK Indus., Inc. (In re DAK Indus., Inc.)*, 66 F.3d 1091, 1094 (9th Cir. 1995).

36. The Debtors' post-petition incurrence of liability to IFIC pursuant to the Bonds and Indemnity Agreement constitutes "actual, necessary costs and expenses of preserving the estate," as contemplated by § 503(b)(1)(A) of the Bankruptcy Code, and as such, should be paid in full. *See In re Crystal Apparel, Inc.*, 220 B.R. 816, 830 (Bankr. S.D.N.Y. 1998) (finding that "[t]ransactions in the ordinary course of business of the debtor-in-possession create expenses of administration").

37. Based on Section 503(b)(1), IFIC is owed an administrative expense claim based on amounts arising out of the Bonds and Indemnity Agreement during the Administrative Claims Period. Since only some of the Bonds were fully released prior to the Administrative Claims Period, IFIC faces exposure for claims that can arising during this period based on the remaining active Bond but also inactive and cancelled bonds. Unlike Bonds that have been fully released, tail exposure lasts for a year after the Bonds are cancelled or, where inactive, the Bonds expire. Thus, there is real risk that Bond claims can be filed that arising the Administrative Claims Period..

38. Indeed, there are already indications such claims are likely. In the Debtors' September 2021 Monthly Operating Report (Dkt. #979), the Debtors show an outstanding balance due to the Dallas Forth-Worth International Airport (one of IFIC's Bond Obligees) for rent. If there are already outstanding amounts due to one Bond Obligee, there is no reason to think there could not be others especially given the lengthy remaining tail exposure.

39. Furthermore, during the pendency of this Chapter 11 bankruptcy, IFIC has incurred Legal Fees. As the Indemnity and Bonds benefitted the Debtors' estates during the pendency of the Administrative Claims Period, associated Legal Fees that were incurred during this period also benefitted the estate.

40. Indeed, the requirement to pay IFIC's Legal Fees was recognized by the Debtors much earlier in the case. In the Final DIP Order, the Debtors agreed to pay IFIC's Legal Fees directly subject to the limitation set forth in Section 26(b) of the Final DIP Order. *See* Final DIP Order, § 26. As set forth in Exhibit A, the exposure under the Bonds far exceeds the amount that would permit the Debtors to rely on the 26(b) limitation to its exposure. Thus, IFIC has an administrative claim for Legal Fees, premiums and Bond claims that arose during the Administrative Claims Period.

RESERVATION OF RIGHTS

41. The submission of this Objection by IFIC is not intended as, and shall not be construed as: (a) IFIC's admission of any liability or waiver of any defenses or limitation of any rights of IFIC with respect to any claims against any one or more of the Bonds or under any indemnity agreement in favor of IFIC, including the Indemnity Agreement; (b) IFIC's waiver or release of any right to exoneration it may have against anyone with respect to any of the Bonds; (c) IFIC's waiver or release of its right to be subrogated to the rights of one or more of the parties paid in connection with the Bonds;

(d) an election of remedy; or (e) consent to the determination of any of the Debtors' liability to IFIC by any particular court, including, without limitation, the Bankruptcy Court.

42. IFIC reserves the right to object and put forth any argument in relation to any motion filed by the Debtors for the Bankruptcy Court's authorization of assumption and assignment of executory contracts and unexpired leases, and to raise any arguments by any other party in their objection(s) to the Amended Plan.

43. IFIC expressly reserves, and does not waive, any and all of its rights, claims, defenses, limitations, and/or exclusions in connection with its and any of the Debtors' or its affiliates' rights and obligations under any Indemnity Agreement, the Bonds, applicable law, or otherwise. IFIC further reserves all rights to assert any and all such rights, claims, defenses, limitations and/or exclusions in any appropriate manner or forum whatsoever (including, without limitation, any of its rights to have any non-core matter relating to the interpretation of its contractual rights and Debtors' contractual obligations adjudicated by the United States District Court).

44. IFIC further reserves all of its rights to raise any issues contained in this Objection and any other related issues in any procedurally appropriate contested matter and/or adversary proceeding, including, without limitation, (i) objections to confirmation of any future revision to any plan including the Amended Plan (ii) a separate adversary proceeding requesting any appropriate declaratory and/or injunctive relief; (iii) or an objection to any subsequent motion seeking approval of an asset sale to any prospective asset purchaser with respect to any contractual rights that may be adversely affected by a sale motion or the confirmation of any plan including the Amended Plan.

MCELROY, DEUTSCH, MULVANEY
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Dated: December 4, 2021

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